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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

No. 288

SID W. RICHARDSON, ET AL

Petitioners,

VS.

KEITH KELLY, RECEIVER,

Respondent.

Reply to Respondent's Brief in Opposition to the Petition for Writ of Certiorari

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TO THE HONORABLE, THE SUPREME COURT OF THE UNITED STATES:

Respondent's reply to the petition for writ of certiorari raises in limine the absence of any real Federal question for this Court's determination. The argument in this connection inaccurately states the Petitioner's contentions, misconstrues the decision of the Supreme Court of Texas in the case at bar and on the whole is misleading to such extent as to require reply on our part.

We respectfully request the court to permit this reply for fear that silence on our part would be taken as an endorsement of the statements made and conclusions reached in respondents' argument.

PRELIMINARY STATEMENT

Respondent precedes the argument of his counterpoints by a "Statement of the Case," in which he asserts that the judgment in the assessment suit, Cause No. 63621, was *in rem* and not *in personam;* that such judgment contains recitals as to the court's jurisdiction; that under state law such a judgment is conclusive until set aside on direct attack; that in such an attack it is incumbent to establish the existence of a meritorious defense; and that the Courts of Texas have held in the case at bar that petitioners have no defense.

In the first place this court has held that suits such as the one at bar are *in personam* and not *in rem.* The Texas cases *(Clay v. Moore,* 175 S. W. (2d) 433 and *McLean v. Morrow,* 137 S. W. (2d) 113) cited by respondent at page 3 in support of his statement that the suit is *in rem,* do not so hold and if they did the holding would conflict with this court's holding in *Christopher v. Brusselback,* 302 U. S. 500. See also *Partridge v. Martin,* 102 F. (2d) 284, *Cert. Den.* 307 U. S. 644.

Secondly the pronouncement that the courts' recital as to its jurisdiction in the judgment in Cause 63621 is conclusive and can be avoided only by a di

rect attack in which a meritorious defense is proved is a broadside proposition that begs the question actually at issue and depends for validity on an erroneous premise—viz: that the recitals in the judgment concerning the class defendents are conclusive regardless of the constitutionality of the use in such a case of the class action device.

The judgment in 63621 recites that jurisdiction existed over the petitioners and other uncited subscribers *because they were members of a class.* If the class suit was not maintainable as such, then the judgment is void on its face and subject to attack anywhere at anytime without the necessity of showing the existence of a defense thereto. The law of Texas on this point *(Empire Gas & Fuel Co. v. Noble,* Tex. Comm. App., 36 S. W. (2d) 451, 454; *Kern Boche Supply Co. v. Freeze,* 96 TEX 516; *Galveston H. S. & A. Ry. v. War,* 74 TEX 47) does not differ from the rule applied by this court. *Old Wayne Mutual Life Association v. McDonough,* 204 U. S. 8; *Earle v. McVeigh,* 1 Otto (91 U. S.) 503.

The assertion at page 7 of respondent's brief, emphasized by the use of italics, that "petitioners have never contended at any point in this proceeding that the judgment entered in the class suit is void on its face and that they are entitled to set it aside without showing a meritorious defense" is completely refuted by the record.

The petitioners have contended at every step of the case that the judgment in 63621 if held binding upon

them as members of a class deprived them of their property without due proccess.[1]

The Supreme Court of Texas in deciding the case stated (R. 806):

> "Petitioners urge that the judgment in Cause 63621 is void because that suit was not maintainable as a class suit."

Next, Respondent at page 9, repeated at pages 13, 17 and 44, of his brief states categorically that the court below held that petitioners had no defense to the cause of action asserted in cause 63621. This is the keystone in respondents argument—that the case turned on a decision that petitioners had no defense and therefore the decision of the Texas Court is based on an adequate non-federal ground precluding this court's review of the case.

The statement is subject to a fundamental objection. In the Supreme Court of Texas, petitioners urged that the judgment was void (R. 806) or in any event was voidable because of the Receiver's conduct of the litigation. In the event it was held voidable, petitioners urged that they had a defense to the assessment suit. The Supreme Court expressly refused to pass on the question of the defense urged, basing its opinion entirely on the holding that the original

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[1]Petitioner's Second Amended Original Petition, par. 26 (R. 172) Second Point of Appeal in Court of Civil Appeals (R. 751) Fifth Assignment of Error in the Application for Writ of Error to the Supreme Court of Texas (R. 798).

judgment was neither void, nor voidable because of the Receiver's actions.

The opinion of the Texas Supreme Court, in this respect at least, is clear and express. This Court is not constrained to accept either petitioners' or respondents' explanation as to its content. The holding of the Court itself is as follows (R. 816):

> "We hold that the judgment in Cause 63621 was neither void nor voidable, *therefore, it is unnecessary for us to consider other questions raised by petitioners.*"

REPLY TO RESPONDENT'S FIRST, SECOND AND THIRD POINTS

Respondent asserts in Points One and Two that a prerequisite to petitioners case was the establishment of a meritorious defense to the matter litigated in Cause 63621; that the Supreme Court of Texas in the case at bar has held that petitioners have no meritorious defense; that the judgment is, therefore, based on an adequate non-federal ground and beyond the jurisdiction of this Court to review.

Point Three goes one step further, asserting that petitioners do not even contend that they have a defense to the cause of action or that they could prevail in the suit if it should be retried.

The basic premises involved is not included in the propositions asserted but is made in respondent's "Statement of the Case" where it is stated that the

class suit judgment containing jurisdictional recitals concerning the petitioners as class members, is not void, but voidable at best, and that petitioners, therefore, were under the burden of establishing a meritorious defense to the suit before they could set the judgment aside. As pointed out (Page 3, ante) this assertion assumes the very question involved in this petition—the availability of the class action device in the first place. If the class device was not available, then the judgment against petitioners as members of a class was void on its face—a nullity—and the Supreme Court of Texas in refusing to so hold deprived petitioners of their property without due process of law, regardless of the basic validity of their defense to an assessment suit.

Secondly, the respondent asserts that the Supreme Court of Texas has held that petitioners have no defense to the cause of action asserted in the class suit. The premise is false. The Supreme Court deliberately refused to hold that no defense existed (R. 816) and based its holding squarely on the proposition that petitioners as class members were bound by the judgment in cause 63621 and that the judgment was neither void (because of the unconstitutional use of the class action device) nor voidable (because of the fraud of the Receiver in the conduct of the litigation).

Respondent then inaccurately states in Point Three, that these petitioners admit that they have no real defense to an assessment suit and that on a retrial of the case, the same judgment must be entered be-

cause of their inability to present a defense. (Reply Brief, Page 17).

The self-evident fact is that petitioners have devoted six years of litigation with its attendant expense to the proposition that they have a defense to an assessment suit. This case is before this Court on petition because the State Court has held that petitioners are concluded by the class judgment in cause 63621 and that the finality of that judgment bars petitioners from reopening the case to present their defense.

If Respondent intends to assert that there can be no defense to a class assessment suit in Texas, he has ignored the decision in *Hill v. Blanco National Bank*, 179 S. W. (2d) 999, Writ Refused. In the only case in Texas where the original class suit was actively defended by the class defendants and appealed to the higher courts, it was held that the members of the exchange, under the reciprocal insurance law of Texas and under their contracts were not liable for an assessment.

The basic validity of petitioners' defense was not considered nor determined by the judgment of the State Supreme Court (R. 816). It cannot be determined by this Court because it involves no federal question. It is a question to be determined upon a retrial of the case, if the Receiver determines to pursue his alleged right to the assessment.

REPLY TO RESPONDENT'S FOURTH POINT

The argument on this point asserts that a class action is properly maintainable to establish the several liabilities of the members of a reciprocal insurance exchange for an assessment.

This was the exact question determined by the decision of this Court in the Brusselback case (302 U. S. 500). In that case the statute imposed on the shareholders of the bank an additional and contingent liability, but the liability so imposed was *several.* To the extent that the identical liability existed as to each and every shareholder, the duty owed to the creditors of the bank by the shareholders was *common,* but the existence of this *common* obligation was insufficient to deprive such shareholder of the right to contest every step essential to the judicial determination of the asserted liability against them severally and as individuals.

The statement at page 21 of respondent's brief that the State Supreme Court has held in *Sergeant v. Goldsmith Dry Goods Co.,* 110 TEX 482, 221 S. W. 259, that the members of a reciprocal insurance exchange are *jointly* and *severally* liable for claims of third parties is inaccurate. The insurance company in the case cited by respondent was organized and the activities giving rise to the ltigaton involved, occurred prior to the enactment of the reciprocal insurance laws of Texas. In the case of *Hill v. Blanco National Bank,* 178 S. W. (2d) 999, Writ of Error Refused, it is held that the decision in *Sergeant v. Gold-*

smith Dry Goods Company does not apply to reciprocals organized as such under Title 78, Chapter 20, Revised Civil Statutes of Texas, and that no joint liability exists against the members of such an exchange for any class of claims. Even the Receiver in Cause 63621 did not go this far in his contention and the judgment procured by him was expressly made *several and not joint.* (R. 665).

Respondent in his brief has argued the propriety of the class assessment suit from the decisions of this Court in *Hartford Life Insurance Co. v. IbS*, 237 U. S., 662; *Supreme Tribe of Ben Hur v. Cauble*, 255 U. S. 356 and *Royal Arcanum v. Green*, 237 U. S. 531, none of which are in point as set out by Chief Justice Alexander in the dissenting opinion below.

The rule established by the Brusselback case and *Pink v. AAA Highway Express* is discussed at Page 28 of the Petition and supporting Brief. Briefly restated, the rule is that a class suit to determine the members' liability to assessment may bind absent and uncited members *only if because of statute or their contracts the members have consented to such ex parte determination by accepting membership in the association.*

The existence of a contingent liability is not enough. It is the existence of a statutory or contractual right to enforce that liability by *assessment* that is controlling. *Miller v. Barnwell Brothers*, 137 Fed. 2d 257.

The cases cited by the respondent to support the use of the class suit in this case do not conflict with the general rule. In fact, the cases support petitioner's contention because in each of them, the right to enforce the liability of the members or shareholders by *assessment* existed either by statutory enactment or by virtue of the provisions of the contracts involved. With the distinction in mind, we turn to an analysis of the cases cited.

For example, in the *IBS* case, the certificates of insurance involved provided for the "payment of all assessments duly levied upon all the members to create a mortuary fund."

In *Royal Arcanum v. Green*, supra, Green's application for membership contained an agreement "to make punctual payment of all dues and assessments for which I may become liable and to conform in all respects to the laws, rules and usages of the Order now in force or which may hereafter be adopted."

In *Cauble's* case, while it does not appear from the opinion of the Court, the fraternal insurance organization involved (Supreme Tribe of Ben Hur) undoubtedly had the customary assessment provisions in its by-laws common to such organizations.

In *Mitchell v. Pacific Greyhound Lines*, 91 Pacific (2d) 176, a case involving a reciprocal insurance association organized under the laws of California, the power of attorney involved contained a specific provision concerning assesments, as follows: "We hereby

subscribe, subject to the call of the advisory board, a sum equal to our total basic annual deposit, to pay excess losses incurred under this contract."

In the Texas case, *Southern Ornamental Iron Works v. Morrow*, which is cited as a controlling authority in the majority opinion of the Texas Supreme Court and upon which respondent mainly relies, 101 S. W. (2d) 336, the contract of the members embodied in the power of attorney which each of them executed, contained a provision that "no one subscriber should ever be required to pay by assessment for such deficits and losses a greater sum than an amount equal to one additional annual premium deposit." (Loc. Cit. Page 388).

It can be seen from the foregoing that these cases conform to the principle of law that petitioners here urge. In each of the foregoing cases either the applicable statute or the contracts of the parties *provided for an assessment* as the means of enforcement, so as to authorize the Court in holding that the members, by becoming such, had impliedly consented to an ex parte determination of the necessity for and the amount of an assessment and consequently were bound by a judgment establishing those facts, although they were not parties to the suit.

The statutes of Texas neither impose a liability nor make a provision for an assessment. *Hill v. Blanco National Bank*, supra. Whether the contract of the members did so is readily ascertainable from inspection, the Power of Attorney relied on by the

Receiver and forming the basis of the judgment in Cause 63621 being found in the printed record. (R. 572). We submit that the contract is silent on the subject.

Respondent undertakes to distinguish the Brusselback case on four grounds, which we shall directly answer:

First: The difference in the relationship between stockholders of a corporation and members of a reciprocal insurance exchange, the former being not liable to assessment at all unless made so by statute, the latter, under Texas law, being under a duty to contribute to a fund to discharge claims against the exchange by virtue of their relationship to each other.

In the first place the existence of the corporate relationship and the correlative right of the corporation to stand in judgment for its stockholders has been a stronger force in the decisions of the courts in the so-called class suits than any other factor. In the next place respondent inaccurately states the law of Texas as to the liability of the members of a reciprocal insurance exchange. The case of *Sergeant v. Goldsmith*, 110 Tex, 482, cited by respondent has been held inapplicable to reciprocals organized under the Title 78, Chapter 20 Revised Statutes (see page 8, ante) and the members of such an exchange, are not liable to contribute any sums in excess of their original premiums unless by their contracts they have expressly so provided. *(Hill v. Blanco National Bank*, supra).

The first ground of distinction therefore is not sound.

Second: That the assessment liability of the petitioners constituted an asset of the exchange whereas this fact was not true in the Brusselback case. To support this contention respondent cites *Mitchell v. Pacific Greyhound*, 91 Pacific 2d 176, but in that case as we have pointed out, the members had expressly, by contract, *subscribed such contingent amounts, subject to call*, so that the case could not apply to the facts of the case at bar.

At Page 32 of the Brief the respondent cites *Art. 5029*, Revised Civil Statutes of Texas, 1925, as authorizing an assessment. Our courts have expressly held to the contrary *(Hill v. Blanco National Bank*, supra). In that case the court stated:

> "Appellant in his motion reiterates his contention that R. S. Arts. 5024 to 5033, inclusive, imposes assessment liability on the subscribers in the reciprocal exchange here involved. Without extended discussion, this court is constrained to adhere to its former opinion holding to the contrary."

Respondent then contends that Sec. 15, 16(a) and 23 of Art. 8308, R. C. S. 1925 (the Workmen's Compensation Statute of Texas) provide the statutory basis for the assessment. These articles of the statute are appended to the reply brief in the appendix thereto.

This contention is briefly answered by stating that reciprocal insurance exchanges are governed by the

provisions of Title 78, Chapter 20 of the statutes, comprising Arts. 5024 to 5033, the last cited article reading as follows:

> "Except as herein provided no insurance law of this state shall apply to the exchange of such indemnity contracts unless they are specifically mentioned."

The Workmen's Compesation law of Texas is divided into four parts and appears as Articles 8306, 8307, 8308 and 8309 of the Revised Civil Statutes. Section 2 of Art. 8309 provides that any insurance company including reciprocal companies shall have the right to issue Workmen's Compensation policies and when it does so it shall be "subject to the provisions of Parts 1, 2 and 4 and of Sections 10, 17, 18(a) and 21 of Part 3, (Art. 8308) of this law.

It is at once apparent that reciprocal insurance companies are not subject to the provisions of Section 15, Section 16(a) and Section 23 of Art. 8308 as contended by the respondent.

The second ground of distinction is therefore not sound.

Third: That petitioners had warning that their respective liabilities to assessment might be determined by class suit by reason of the decision in *Southern Ornamental Iron Works v. Morrow* decided by the Court of Civil Appeals in 1937 (101 S. W. (2d) 336).

This argument would bind petitioners to the result of *Southern Ornamental Iron Works v. Morrow* re-

gardless of the correctness of that decision when measured by the requirements of the 14th Amendment. In effect the argument urges that this Court and petitioners are bound by the determination of the State Court on an interpretation of the Federal constitution, whether it conflicts with the interpretation given it by this Court or not. Of course this Court could not be bound thereby. *Coombs v. Getz*, 285 U. S. 434, 441; *Larson v. South Dakota*, 278 U. S. 429; *Appleby v. City of New York*, 271 U. S. 364; *Stearnes v. Minnesota*, 179 U. S. 223, 232. Neither, we submit, could petitioners who had no part in that case and could not have appealed it to this Court on the constitutional question involved under the due process clause.

If the case has the force ascribed to it by respondent, it conflicts with this Court's later decision in the Brusselback case. Confined to its own facts, however—a case involving a contract under which each subscriber not only agreed to a contingent liability, but on *an assessment as the means of enforcement*, (101 S. W. (2d) 338), *Southern Ornamental Iron Works v. Morrow*, can be reconciled with rule of this Court announced by Chief Justice Stone in the Brusselback case, *Pink v. AAA Highway Express* and *Hansberry v. Lee*.

In either event the distinction which respondent seeks to draw is not tenable.

Fourth: Respondent next asserts that the Brusselback case is inapplicable because it did not involve a

true class suit. A reading of the opinion would indicate that the primary contention in the case was that under Equity Rule 38 the Illinois judgment was conclusive on all stockholders, whether served in the proceeding or not and this Court passed on that question, holding that notwithstanding Rule 38 the judgment could not be binding on absent and uncited shareholders.

But there can be no debate concerning the type of suit involved in *Partridge v. Martin*, 102 Fed. (2d) 284, Cert. Den., 307 U. S. 644. It was a deliberately contrived, all inclusive, class action brought to exploit what counsel evidently thought was a loop-hole in the Brusselback case. The 8th Circuit Court held the decree not binding on absent and uncited shareholders under the authority of the Brusselback case and this Court denied the petition for certiorari and refused to review the holding.

We submit the fourth ground of distinction is therefore invalid.

REPLY TO RESPONDENT'S FIFTH POINT

It is argued that the courts below have held that the Receiver Kelly properly conducted the class suit. To the contrary we say that no court yet has directly held that Kelly's conduct was not improper. An implied finding in the face of the undisputed facts in the case cannot stand and the courts below have not based their decision in this case on any such finding.

We can add nothing to the matter outlined in our original brief. The facts are stated by the witnesses Rogers, Holloway, Evans, Gresham and the Receiver Kelly. The essential facts are undisputed that Kelly made an agreement with Rogers, Holloway and Evans under which they were given settlements in consideration of not further contesting the case (original Brief Page 33-43).

The hard fact cannot be passed by saying that there was substantial evidence to base a holding that no fraud was shown to exist. Even the majority opinion of the court below did not go so far. It escaped the proof by ignoring it. The court referred to the recitation in the original class judgment to the effect that the 3200 members of the class were "fairly and truly represented herein by the named defendants," and then held the recitation conclusive in spite of the fact that Kelly himself prepared the judgment (R. 245) and the trial court could not have had any knowledge of the out-of-court negotiations reflected above.

Respondent's real contention is that the Receiver's fraud in the conduct of the class suit was harmless error because petitioners were bound to lose the case in any event. Such logic would destroy the fundamental requirement of the due process clause that a class suit to be valid must be fairly, honestly and openly tried.

CONCLUSION

We respectfully submit that this Court has jurisdiction to determine the constitutional question presented by the petition and that the petition should be granted as prayed for.

Respectfully submitted,

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